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IN THE

Supreme Court of the United States

No. 70.

October Term, 1947.

GILES KAVANAGH, Collector of Internal Revenue,
Petitioner,

v.

J. H. NOBLE,
Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

BRIEF FOR THE RESPONDENT.

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No. 70. OCTOBER TERM, 1947.

GILES KAVANAGH, COLLECTOR OF INTERNAL REVENUE,
Petitioner,

v.

J. H. NOBLE,
Respondent.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

BRIEF FOR THE RESPONDENT.

OPINIONS BELOW.

The opinion of the District Court for the Eastern District of Michigan is reported in 66 F. Supp. 258, and the affirming opinion of the Circuit Court of Appeals for the Sixth Circuit in 160 F. (2nd) 104.

QUESTION PRESENTED.

The statement of the question appearing on page 2 of the petitioner's brief can have no application to the facts in the instant case. The real question presented in this case is whether claims for refund of illegal collections, claimed to be income taxes but which the Congress had never imposed, must be filed within two years after the payment of the tax as provided by Section 322 (b) of the Internal Revenue Code or within four years after the payment of the tax as provided by Section 3313 of the Internal Revenue Code (R. S. 3228).

STATUTES AND REGULATIONS INVOLVED.

Internal Revenue Code, Section 322, so far as pertinent reading as follows:

"(a) (1) *Overpayment.* Where there has been an overpayment of any tax imposed by this chapter, the amount of such overpayment • • • shall be refunded immediately to the taxpayer • • •

(b) (1) *Period of limitation.* Unless a claim for credit or refund is filed by the taxpayer within three years from the time the return was filed by the taxpayer or within two years from the time the tax was paid, no credit or refund shall be allowed or made after the expiration of whichever of such periods expires the later • • •"

Code Section 3313 (R. S. 3228):

"All claims for the refunding or crediting of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty alleged to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected must, except as otherwise provided by law in the case of income, war-profits, excess-profits, estate, and gift taxes, be presented to the Commissioner within four years next after the payment of such tax, penalty, or sum."

Regulations 86, Art. 117-5—Set out *below* in letter from Internal Agent in Charge, dated June 11, 1937.

STATEMENT OF FACTS.

The statement in petitioner's brief is accepted with the addition following page 3 of that brief that the letter from Internal Revenue Agent in Charge to the respondent contained the following statement:

"In completing the audit of the return, it was found that you had failed to comply with the provisions of Article 117-5, Regulations 86. Article 117-5 reads as follows:

> 'In the application of Section 117, a husband and wife regardless of whether a joint return or separate returns are made, are considered to be separate taxpayers. Accordingly, the limitation under Section 117 (d) on the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets.'

When this provision is applied to the sales of stocks, Mrs. Noble has a net loss of $49,862.56, of which $2,000.00 is deductible, and you have a net gain of $45,049.45" (R. 17-18).

Also the further statement that on December 9, 1940, this Court in *Helvering v. Janney, et al.*, 311 U. S. 189, held that Art. 117-5, Regulations 86, quoted in the foregoing letter, was void.

PREFACE.

Petitioner's brief was not mailed to respondent's counsel until October 28, 1947, which may cause a short delay in filing this brief.

The petitioner's brief contains only the usual formal parts, a statement of what purports to be the question presented and a statement of facts. There is no argument and no citations of authorities and it is believed it does not constitute such a brief as contemplated in the rules of this Court.

The purported brief in lieu of argument refers to a brief filed in a case appearing as No. 71 on the docket, which has not been consolidated with the instant case and

is totally unlike it in all the pertinent facts involved and none of the parties are the same. A careful study of that brief discloses that it is not material to the issue in the instant case which involves no income tax.

Throughout the certiorari proceedings in the present case there has been evident the plain intent to make the fight in case No. 71, *Jones, Collector v. Liberty Glass Co.* and then undertake to attach the instant case as an appendage to that case, though there is no similarity in the facts in the two cases.

In the petition for the writ of certiorari in the instant case no reasons were assigned for invoking the jurisdiction of this Court but only a reference to a petition filed in the *Liberty Glass Co.* case.

While amounts in dispute are usually immaterial to legal points involved it may be noted that in the petition for certiorari in the *Liberty Glass Co.* case one of the reasons given for the grant of the writ was the importance of the case involving other cases, it was stated, amounting to approximately $200,000.00, which sum was "no measure of the amount of refunds that would have to be made, etc.", and yet the fight is being made on a little claim for $1,053.49 instead of being made in the instant case involving a refund of $21,105.90 because of a sum exacted by the Commissioner and collected by the petitioner without authority of law and under a Regulation which this Court declared invalid.

The Court is respectfully requested to refer to the respondent's motion to dismiss the writ of certiorari with its supporting brief in which there are pointed out the dissimilarities and contrasts between the two cases now endeavored to be yoked together.

It is believed that in the progress of this case the facts both as to treatment in the petition for the writ and in the brief and in the total dissimilarity between the two cases will warrant the dismissal of this proceeding.

SUMMARY OF ARGUMENT.

The exceptive clause in Revised Statutes 3228 embraces only the cases stated in the exception. The statutory language used in Code Section 322 may not be enlarged so as to embrace refunds of taxes not "imposed by this chapter."

The facts in this case do not bring it within the limited application of the language used in Section 322 and this has been the view of all the lower courts who have passed upon the question in similar cases where collections were made as of taxes that the Congress had not imposed as distinguished from those cases where too much of a lawfully imposed tax had been paid.

The historical development of the exceptive clause in R. S. 3228 and of Code Section 322 support this position.

This is particularly a case for the application of R. S. 3228 in that the respondent had paid all taxes for the year involved that had been imposed upon him by law and there should not have been exacted from him under an illegal and void regulation the sum of money the petitioner collected from him purporting to be a tax on his gains from sales of capital assets, disregarding his wife's losses though a joint return had been filed.

ARGUMENT.

The issue is simply stated, whether the collection in this case was a tax imposed by the income tax provisions of the revenue laws, refund of which would be governed by Code section 322 (b), or a collection, not of any tax imposed by such income tax provisions, but an illegal collection made without authority of law, refund of which is governed by Code section 3313 (R. S. 3228).

This is not an income tax case. None of the laws relative to income taxes can have application here. It might as well have been called a gift tax, a transfer tax, or any excise tax, calling it so does not make it so. Suppose the

Commissioner had called it an estate tax, would the limitation on refunds of estate taxes apply?

The revenue laws as enacted by the Congress provide for a joint return of husband and wife as a taxable unit and impose taxes on the income of such taxable unit, and it was so held by this Court in the *Janney* case (*supra*).

The respondent and his wife made such authorized joint return in which was reported their joint income as such taxable unit and paid the tax assessed on such return, and a small deficiency later determined (R. 17 (6)). Thereupon all duty of this taxable unit—including both husband and wife—as to the year 1935 ceased. All legally required return had been made. All taxes imposed by law had been paid. The amount here involved was collected on transactions that produced no income, that resulted in a loss, something never authorized by the Congress nor by the Sixteenth Amendment.

I.

The Exceptive Clause in Revised Statutes 3228.

It is well recognized that an exception in a general statute is to be strictly construed, and that courts will not curtail the general provision nor add to the exception by implication, that the language of the exception defines the extent of its force.

Further, this Court has particularly stated:

> "In the interpretation of statutes levying taxes it is the established rule not to extend their provisions, by implication, beyond the clear import of the language used, or to enlarge their operations so as to embrace matters not specifically pointed out. In case of doubt they are construed most strongly against the government, and in favor of the citizen." *Gould v. Gould*, 245 U. S. 151.

This principle applies to statutes of limitations. *U. S. v. Updike*, 281 U. S. 489.

The language in the exceptive clause and the language in the thing excepted should determine the issue.

The historical development of this exceptive clause is exhaustively set out by Judge Haney in the opinion of the Circuit Court of Appeals of the Ninth Circuit in *Huntley v. Southern Oregon Sales, Inc.*, 102 F. (2nd) 538, where it was held that Code Section 322 has no application in the matter of refund of a collection made as for an income tax but where no such income tax had been imposed by law.

The withdrawal of legally imposed income taxes from limitation provisions of section 3228 of the Revised Statutes first appeared in section 1316 of the Revenue Act of 1921 amending R. S. 3228 by adding thereto the following paragraph:

> "This section except as modified by Section 252, shall apply retroactively to claims for refund under the Revenue Act of 1916, the Revenue Act of 1917 and the Revenue Act of 1918."

The "modification" of section 3228 R. S. provided by "Section 252" of the Revenue Act of 1921 referring to excess payment of taxes imposed by the named Acts was changed in the Revenue Act of 1924 to "Section 281" because that was the section providing for limitations of refunds where there has been an overpayment of any income tax • • • "imposed by this Act" or prior Acts, and likewise in the Revenue Act of 1926 this exceptive clause referred to "Section 284" of that Revenue Act because of the change in section numbers in the income tax title of the act, and then, apparently to obviate the need for the continued change of section numbers, the wording of the exceptive clause was changed to "except as otherwise provided by law in the case of income,—war-profits, excess-profits, estate and gift taxes."

There appears to be no other significance, and it is believed none is claimed, in the changes in the wording of

this exceptive clause, the clause in meaning going back to the Revenue Act of 1921 adding to R. S. 3228 the clause "except as modified by section 252."

The Congress always qualifies and limits this exceptive clause, "except as modified by Section 252" (1921 Act), "except as provided in Section 281" (1924 Act), "except as provided in Section 284" (1926 Act), "except as otherwise provided by law in the case of income, etc., taxes" (1928 and subsequent Acts, and Code Sec. 3313).

Never even was there a general exception of all income taxes, but always qualified as above.

When the Congress wanted to except all income taxes from the operation of any statute it had no difficulty in saying so. For instance, it was desired that Code section 3312 should not apply to income, etc., taxes at all. Consequently that section reads, "except in the case of income, etc., taxes * * * all internal revenue taxes shall, etc., be assessed within four years after such taxes became due * * *".

If the Congress had meant to except not only those cases provided for by certain sections—afterwards changed to the more embracing term "law," but for all refunds of income, etc., taxes, it could so easily have said so by saying:

> "Except in the case of income, etc., taxes all claims for the * * * refunding of any internal revenue tax alleged, etc."

Just as was done in enacting Section 3312 so as to eliminate income taxes from the limitation of that section. But it didn't say that. Obviously it didn't mean that. It didn't mean to except all income taxes but only those otherwise provided for, only those imposed by law.

It is well settled that "there is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes." *U. S. v. American Trucking Association*, 310 U. S. 534, 543.

A study of the historical development of this exceptive clause and of the provisions for the refund of excess payments of taxes legally imposed still further indicates that the Congress meant what it said when it "undertook to give expression to its wishes."

II.

The Limited Statutory Application of Code Section 322.

This limitation so far as pertinent here originally appeared as Section 252 of the Revenue Act of 1921 providing a limitation on claims for refund of five years from the time the return was filed where it appeared "upon examination of any return of income made *pursuant to this Act*" (emphasis ours) that an amount of tax had been paid in excess of that properly due, although that five year period might exceed the general limitation in R. S. 3228.

Then arose the doubt as to whether a claim for refund of an ordinary overpayment of a lawfully imposed tax paid after the expiration of the five year period from filing a return could come within the application of R. S. 3228 providing for refunds of *illegal* collections, not of too large payment of a lawfully imposed income tax.

In this connection the petitioner, in the courts below, cited the Mellon letter and the Gregg statement as illustrating the need of amendment.

Thereupon was enacted the Act of March 4, 1923 (C. 276,42 Stat. 1504) amending this section 252 of the 1921 Act by inserting a limitation of two years after payment on refunds of excess payments of lawfully imposed taxes.

In section 281 of the 1924 Act, 284 of the 1926 Act and 322 of the 1928 and subsequent Acts the application of these sections is always limited to tax "imposed by this Act", and other named Acts, "imposed by this Title", or "imposed by this chapter" (Code Sec. 322).

Always the tax must have been imposed by law before this section would apply.

The use of the word "overpayment" in these sections providing for limitations on refunds of lawfully imposed taxes seems to be of no special significance. The material words are—"tax imposed by this chapter."

Besides in Section 4 (c) of the Current Tax Payment Act of 1943, now codified as Code Section 3770 (c) immediately preceding section 3771 relating to "interest on overpayments", it is provided:

> "(c) *Rule Where No Tax Liability.*—An amount paid as tax shall not be considered not to constitute an overpayment solely by reason of the fact that there was no tax liability in respect of which such amount was paid."

This would seem to dispose of the contention made by the petitioner in the courts below that respondent's position would deny interest on overpayments and defeat the jurisdiction of the Tax Court.

III.

The Facts in This Case Do Not Bring It Within the Limited Application of Code Section 322.

There could not have been any "tax imposed by this chapter" on the respondent's gain of $45,049.45 on his sales of capital assets because where a joint return is filed there is no tax on one spouse as an individual.

There could not have been any "tax imposed by this chapter" against the taxable unit of husband and wife on capital sales, as they resulted in a loss. The Commissioner undertook to impose a tax on a loss.

The question is, whether the Commissioner imposes the claimed liability or whether the law imposes it, and under its terms Code section 322 applies only to the latter.

The collection of this money by the petitioner was his individual act. He was personally liable. He was personally sued. The United States did not collect the money

from the respondent. The petitioner's act in making the collection was unauthorized by any law, unauthorized by any official with lawful power to order the collection made. Code section 322 could not apply to the petitioner, he did not collect a "tax imposed by this chapter", a tax imposed by the United States or authorized by the United States.

IV.

The Views of Lower Courts.

The decisions of other courts in comparable cases, and the sound reasoning in the opinions in the courts discussing the question at length, and the unanimity of the conclusions reached, would seem of persuasive value.

First was the *Southern Oregon Sales, Inc.*, (*supra*) case affirming the district court in a lucid and thorough discussion of the question.

In that case the Solicitor General formally announced that no petition for certiorari would be filed (1939 Prentice-Hall Federal Tax Service, Sec. 4.35).

Since that decision in 1939 the Congress has passed nine revenue acts affecting income taxes and no change was made as to limitations on refunds of illegal collections as construed by that court.

Thus it may be implied that the court's construction of the statutes met the approval of the Congress.

In *U. S. v. Lederer Terminal Warehouse Co.*, 139 F. (2nd) 679, the Circuit Court of Appeals for the Sixth Circuit affirming the district court, cites the *Southern Oregon Sales., Inc.*, case, with approval and follows up the historical development of this exceptive clause, adding the statement:

> "The fact that in the cited case, *no tax whatever* was due from the taxpayer while in the instant case, *no additional tax was due* is deemed immaterial." (Emphasis the court's.)

However in the case at bar no tax whatever was due, the legal tax liability having been fully paid (R. 17 (6)).

In the *Lederer* case the court said:

> "Congress evidently considered that less time would be required for the discovery of errors in tax returns resultant from miscalculations or mere overpayment than would be required to ascertain the *erroneous or illegal nature of an assessment.* Hence, the inference is logical that Congress intended to allow the taxpayer a longer time to determine whether he had been erroneously or illegally assessed than would be permitted him for the discovery of a mere overpayment of taxes, *assessed and collected upon a correct or legal basis.* This would explain the longer time limitation provided by Congress in Section 3313 than allowed in Section 322 of the Internal Revenue Code." (Emphasis supplied.)

Barring the two dissimilar cases pending in this Court, this case and No. 71, so far as careful study discloses, there have been reported only two other cases involving the question as to whether the two year or the four year limitation applies where sums have been collected which the Commissioner claimed to be income taxes, to wit: *Olsen v. U. S.*, 32 Fed. Supp. 276 (D. C. S. D. California) and *Sbarbaro v. United States*, decided May 29, 1947, (U. S. D. C. N. D. Ill.) 1947 Prentice-Hall Federal Tax Service Sec. 72,485, in both of which cases the collections were held illegal and the four year limitation applied.

It would seem of persuasive value that these four courts reached the conclusion, two of them after exhaustive investigation, as well as the other two district courts in the *Southern Oregon Sales, Inc.*, case and the *Lederer* case, that collections of sums not imposed by law as income taxes are not governed by Code section 322 but by Section 3313, the lower courts in the instant case reaching the same con-

clusion. The unanimity of opinion of the seven courts, five district courts and two circuit courts of appeal passing on the question, it is believed, will receive careful consideration.

When this case was before the Circuit Court of Appeals the petitioner cited *Central Hanover Bank & Trust Co. (Arnold Estate) v. U. S.*, (67 F. Supp. 920) as deciding to the contrary, but that court did not so hold. It only mentioned that in that case the two year limitation applied, as it does to almost all claims for refunds of income taxes, but no holding was made on that point.

In that case there was no collection made under any illegal ruling of general application such as was the fact in the instant case, but the Commissioner had merely made a mistake in cost of certain securities. That was the very kind of case, being an overpayment of *tax imposed by law*, that section 322 was meant to cover. That case was decided in favor of the taxpayer under IRC Sec. 3801 (b) (5) which again illustrates the fact that the Congress has been liberal in its provisions of the time within which to file claims for refund whenever a considerable length of time was necessary in the interest of justice.

V.

Regulations 86, Art. 117-5.

The collection in this case was specifically made under Article 117-5 of Regulations 86 (Under 1934 Act), which is quoted in the letter of June 11, 1937, from the Internal Revenue Agent in Charge asserting this claim against the respondent.

In *Helvering v. Janney, et al.*, (*supra*) this Court held that regulation illegal.

It necessarily follows that the sum now sued for, having been collected under a Regulation of the Commissioner invalidated by the Supreme Court was an illegal collection and that consequently Internal Revenue Code, section 3313,

controls and the period for filing a claim for refund was four years after payment.

This Regulation had been promulgated by the Commissioner with the approval of the Secretary of the Treasury, and though illegal and void, taxpayers were forced to abide by it.

The Commissioner with the approval of the Secretary of the Treasury persisted in this ruling through *Regulations 101, Art. 117-5* applicable to the Revenue Act of 1938, and *Regulations 103, Art. 19.117-5* applicable to the Internal Revenue Code, and until the Supreme Court on December 9, 1940, in the *Jauney* case (*supra*) held that said regulation was illegal, and thereafter on July 2, 1941, the Commissioner by *Treasury Decision 5057* amended the prior Regulations so as to make them conform to the decision of the Supreme Court. Thus for approximately seven years the Commissioner with the approval of the Secretary of the Treasury persisted in making and repeating this illegal ruling so that the same appeared to have the effect of law commanding the respect of all taxpayers.

Surely the exacting of money claimed as a tax but collected under this long persisted in ruling was not such a payment as contemplated by the Committee on Ways and Means in its Report (*H. Rep. No. 1424, 67th Cong. 4th Sess.*) where it was stated that the Committee "considers one year sufficient" (or 2 years as later amended) within which to file a claim for refund.

Throughout revenue legislation there has been manifest the desire and intent of the Congress to allow a taxpayer a reasonable length of time within which to ascertain and determine his right to file a claim for refund.

For example, in the Revenue Act of 1942, section 322 of the Code was amended so as to allow seven years in which to file a claim for refund in connection with the effect that deductibility of a debt or loss has on application by the taxpayer of a carryover, thus giving the tax-

payer a reasonable time for ascertaining and determining his right to file a claim for refund.

Similarly in Public 291, 79th Con. 1st Session approved July 31, 1946, the time for claiming credit or refund with respect to war losses was extended, obviously for the reason that more time was required in which to ascertain and determine the effect of these losses.

Two years within which to file a claim for refund of a collection, enforced through an illegal ruling of the Commissioner, a ruling applicable not merely to that case but generally to all cases similarly situated, would not seem sufficient within which to obtain an adjudication that the ruling was illegal, and this limitation would be thoroughly out of harmony with the clearly and repeatedly shown intent to allow the taxpayer a reasonable time *after the occurrence* within which to determine his rights.

VI.

Statutory Authority for Refunds of Income Taxes Under R. S. 3228.

The Act of March 4, 1923, (C. 276,42 Stat. 1504) amended the Revenue Act of 1921 in the exact language reported by the Committee on Ways and Means to the 67th Congress, 4th Session (Report 1424), and by the Senate Finance Committee (S. Rep. 1137, 67th Congress 4th Session) as follows:

> "(b) Where a tax has been paid under the provisions of section 221 or 237 in excess of that properly due, any refund or credit made under the provisions of this section or section 3228 of the Revised Statutes shall be made to the withholding agent unless the amount of such tax was actually withheld by the withholding agent" *42 U. S. Stat. at Large 1504-5.*

This amendment covered refunds of excess payments of taxes imposed by the Revenue Act of 1921 and by all

prior Acts, but was remedial and applied only to claims thereafter filed.

Sections 221 and 237 were income taxes. Refunds could be made either under section 252, referring to overpayments of taxes imposed by Title I of that Revenue Act or under section 3228 R. S. referring to illegal collections where the amount withheld as tax had not been imposed by law. A close search of the records reveals no report and no enactment changing that intent of the Committees and of the Congress. The meaning of the language is clear and needs no interpretation. It must be that the Committees and the Congress meant what they said.

CONCLUSION.

The decision of the court below is in consonance with the congressional committee reports and with all the courts that have passed on the question, follows the law as enacted by the Congress, and should be affirmed.

Respectfully submitted,

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ADDENDUM — There is no administrative difficulty to be resolved. The Bureau has no difficulty in drawing the distinction between "legally collected taxes" and "illegally assessed and collected taxes" and provides in Mimeograph 3958 (C.B.XI-2,23) and Mimeograph 4564 (C.B. 1397-1,93) that refunds of taxes *"legally collected"* shall be treated as income for the taxable year in which the refund is made, while a different treatment is provided in the case of a refund of *"taxes illegally assessed and collected"*. Applying the same distinction, *"legally collected taxes"* come within the provisions of Code section 322 while *"illegally assessed and collected taxes"* come within the provisions of Code section 3313 (R.S. 3228). The two statutes say so.